

**IN THE UNITED STATES DISTRICT COURT  
FOR THE EASTERN DISTRICT OF PENNSYLVANIA**

<b>UNITED STATES OF AMERICA,</b>	:	<b>CIVIL ACTION</b>
<b>Plaintiff,</b>	:	
<b>v.</b>	:	
	:	
<b>ROBERT J. BIRCH,</b>	:	
<b>Defendant and Third-Party</b>	:	
<b>Plaintiff,</b>	:	
<b>v.</b>	:	<b>No. 10-1212</b>
	:	
<b>PENNSYLVANIA HIGHER</b>	:	
<b>EDUCATION ASSISTANCE AGENCY,</b>	:	
<b>Third-Party Defendant.</b>	:	

**FINDINGS OF FACT AND CONCLUSIONS OF LAW**

**NORMA L. SHAPIRO, J.**

**April 30, 2013**

Plaintiff, the United States of America, Department of Education (“DOE”), filed this civil action against defendant Robert J. Birch (“Birch”) to recover payments for a consolidated student loan with a principal amount of \$60,689.73, plus interest of \$27,552.94, for a total of \$88,242.67. Birch filed a third-party complaint against the Pennsylvania Higher Education Assistance Agency (“PHEAA”) for allegedly breaching a settlement agreement with Birch. The court held a non-jury trial to determine: (1) the total amount of loan money owed by Birch and how much he paid; (2) the amount of collection costs and interest owed by Birch; (3) whether his consolidated student loan was rehabilitated after it was in default; and (4) whether Birch owes the outstanding loan payments to DOE or PHEAA.

The court appointed Jerome Allen Kellner, a certified public accountant, as Special Master in this action (“Special Master Kellner”). The court ordered Special Master Kellner to

review a transcript of the trial and all admitted exhibits and submit a report concerning Birch's student loan history. The court received a draft report, dated December 16, 2011, thereafter. The court then made limited findings of fact regarding Birch's student loan history and directed Special Master Kellner to revise his report in light of the court's findings. Special Master Kellner submitted a revised report. On March 21, 2013, at a hearing on the record, the parties were able to question Special Master Kellner about his report.

In accordance with Fed. R. Civ. P. 52(a), below are the court's findings of fact and conclusions of law.

### **I. Findings of Fact**

On February 10, 1996, Birch executed a promissory note to secure a consolidated student loan guaranteed by PHEAA and reinsured by DOE. The terms of the promissory note provided for payment of a principal amount of \$52,994.28 at a 9% interest rate, to be paid in monthly installments of \$423.43 over a thirty-year period, for a total of \$152,434.08 (principal plus interest in the amount of \$99,439.80). Birch agreed that \$52,994.28 was an estimate and that he would make payments based on the actual amount of the consolidated loan upon disbursement. The amount disbursed was \$55,138.91.

As of May 23, 1997, Birch's consolidated loan was in default because he had not made any payments. The loan holder filed a claim with PHEAA for \$60,689.73 (\$55,138.91 in principal plus \$5,550.82 in interest).<sup>1</sup> PHEAA paid the loan holder \$59,475.94. PHEAA then submitted a reinsurance claim to DOE and was reimbursed by DOE in the amount of \$58,286.42.

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<sup>1</sup> Upon consolidation, the \$5,550.82 in interest was capitalized to the loan's principal balance as required by 34 C.F.R. § 682.410(b)(4).

Interest at the rate of 9% continued to accrue on the unpaid principal amount of \$60,689.73 as required by 34 C.F.R. § 682.410(b)(3).

In June 2002, Birch settled an underlying litigation with PHEAA in the Court of Common Pleas, Montgomery County. The settlement agreement between Birch and PHEAA, effective September 5, 2002, provides, concerning the consolidated student loan:

[Birch must] voluntarily remit 12 consecutive payments of \$600.00—no more than 30 days apart—to AES PHEAA . . . beginning on July 15, 2002, even if such date precedes the full execution of this agreement. Upon remitting the 12th payment, Mr. Birch will contact AES PHEAA . . . to request the rehabilitation of the Consolidation Loan. . . . If Mr. Birch successfully rehabilitates this debt, AES PHEAA agrees to waive all collection fees from the date of rehabilitation forward. . . . If Mr. Birch follows the above mentioned steps, and remits not less than \$600.00 monthly with each payment arriving at PHEAA, not less more [sic] than 30 days apart, PHEAA guarantees that Mr. Birch will qualify for rehabilitation.

Birch agreed to make twelve consecutive payments of \$600, in consideration for which PHEAA would rehabilitate Birch's defaulted loan and waive all collection costs from the date of rehabilitation forward.

At trial, the parties disputed whether the settlement agreement between Birch and PHEAA provided that Birch, to have his consolidated loan rehabilitated, had to make twelve consecutive payments of \$600 more than or less than thirty days apart. A typographical error in the settlement agreement provided for Birch to make twelve consecutive payments of \$600 “not less more [sic] than 30 days apart.”

The settlement agreement should be interpreted to mean that Birch was required to remit payments to PHEAA not more than 30 days apart. The rehabilitation provision of the settlement agreement provides, in another section prior to the section with the typographical error, that Birch must remit twelve consecutive payments of \$600 “no more than 30 days apart.” After

Birch and PHEAA entered into the settlement agreement, PHEAA's billing invoices to Birch bear due dates of the 15th day of each month for Birch's \$600 payment. Birch also alleged, in his third-party complaint, that the terms of the settlement agreement required him to make twelve consecutive payments of \$600 "no more than 30 days apart."<sup>2</sup>

The settlement agreement between Birch and PHEAA provided that the first of Birch's twelve consecutive payments was to be made on July 15, 2002. Birch did not make his first payment of \$600 until September 16, 2002. Birch and PHEAA agreed to allow the September 16, 2002 payment to qualify as the first of the twelve payments necessary to rehabilitate his consolidated loan under the settlement agreement.

Including Birch's initial payment on September 16, 2002, Birch made his twelfth payment of \$600 on October 8, 2003. Birch did not pay invoices due January 15, 2003 and June 15, 2003. Birch's initial twelve payments of \$600 did not occur on a monthly basis, but over the course of fourteen months. Birch did not comply with the terms of the settlement agreement. His loan was not rehabilitated and collection fees were not waived.

After failing to collect the debt from Birch, PHEAA assigned the consolidated loan to DOE on July 3, 2007. PHEAA collected from Birch payments totaling \$45,280.35 between the date of default and the date it assigned its claim to DOE. The payments collected by PHEAA were applied toward collection costs in the amount of \$7,663.43 and interest in the amount of \$37,601.92. The principal amount of \$60,689.73 was never reduced.

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<sup>2</sup> Moreover, if the settlement agreement provided for Birch to make payments "no less than 30 days apart," that provision of the agreement would be illogical, because it would not provide a cap on the time period within which a payment *must* be made. See *Clairton Slag, Inc. v. Dep't of Gen. Servs.*, 2 A.3d 765,773 (Pa. Commw. Ct. 2010) ("A contract should not be interpreted in a way that leads to an absurdity or renders the contract ineffective to accomplish its purpose.").

After PHEAA assigned the loan to DOE, Birch made payments to DOE totaling \$2,232.00. This amount was applied to interest owed, not to principal. As of September 21, 2009, Birch owed DOE \$60,689.73 in principal, plus \$27,552.94 in interest, for a total of \$88,242.67. Interest has continued to accrue on the principal amount at the rate of \$14.96 per day for 365-day years and \$14.92 for 366-day years.<sup>3</sup>

## **II. Discussion<sup>4</sup>**

### **A. The Consolidated Student Loan**

Birch argues that PHEAA and DOE incorrectly applied the payments to his student loan debt. Birch's consolidated student loan was made pursuant to the Federal Family Education Loan Program ("FFELP"), 20 U.S.C. §§ 1071-1087.4. Under FFELP, lenders use their own funds to make loans to students. 34 C.F.R. § 682.100(a); *see United States v. Tuerk*, 2007 WL 916866, at \*1 (E.D. Pa. Mar. 20, 2007), *aff'd* 317 Fed. Appx. 251 (3d Cir. 2009). These loans are guaranteed by nonprofit organizations or state agencies and reinsured by DOE. 34 C.F.R. § 682.101(a).

Under the regulations to the Higher Education Act of 1965 ("HEA"), default occurs when a borrower fails to make payments on a loan for a period of at least 180 consecutive days.<sup>5</sup> 34 C.F.R. § 682.200. Birch defaulted on his consolidated student loan when he did not make any payments for more than a year after signing the promissory note.

In the event a borrower defaults on a loan, the guaranty agency pays the lender and takes

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<sup>3</sup> Special Master Kellner calculated the daily rate utilizing a 365-day year as \$14.9646 and the daily rate utilizing a 366-day year as \$14.9237.

<sup>4</sup> Any facts in the "Discussion" section not found in the "Findings of Fact" section are incorporated by reference therein.

<sup>5</sup> The regulations were amended in 2002 to modify the default period to 270 days. The court will apply the regulations as they existed when Birch obtained the loan.

an assignment of the loan.<sup>6</sup> *Tuerk*, 2007 WL 916866, at \*1. The guaranty agency then files a reinsurance claim with DOE. 34 C.F.R. § 682.102(e)(7). DOE reimburses the guaranty agency for a percentage of the losses it incurred in honoring the default claim. 34 C.F.R. § 682.419(b). PHEAA followed these procedures after Birch's default.

Even after receiving reimbursement, the guaranty agency has a continuing obligation to collect debt from the borrower.<sup>7</sup> *Tuerk*, 2007 WL 916866, at \*1. The guaranty agency must apply payments collected in the following order: (1) collection costs; (2) incidental charges, such as late fees; (3) accrued interest; and (4) principal. 34 C.F.R. § 682.404(f). Collection costs "are reasonable costs incurred by the agency in collecting a loan on which the agency has paid a default or bankruptcy claim," and include, but are not limited to, "all attorney's fees, collection agency charges, and court costs." 34 C.F.R. § 682.410(b)(2). The guaranty agency may charge these collection costs "[w]hether or not provided for in the borrower's promissory note and subject to any limitation on the amount of those costs in that note." *Id.*

PHEAA received \$45,280.35 in payments from Birch between the date of default and the date it assigned its claim to DOE. PHEAA correctly applied this amount first to collection costs (\$7,663.43) and then to interest (\$37,601.92). The principal amount was not reduced because no money remained after PHEAA applied the payments to collection costs and interest.

If the guaranty agency is unable to obtain full payment, it may be required to assign all rights and title in the defaulted loan to DOE. 34 C.F.R. § 682.409(a). The borrower then owes

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<sup>6</sup> When the guaranty agency pays the lender's claim on the defaulted loan, any outstanding interest is capitalized and becomes part of the principal payable to the guaranty agency. 34 C.F.R. § 682.410(b)(4).

<sup>7</sup> The guaranty agency may use various collection methods, including dunning letters, wage garnishment and litigation.

DOE directly. *Id.* DOE may engage in its own debt collection activities. DOE may also recover collection costs and interest and apply payments in that order. 34 C.F.R. § 682.410(b); *see United States v. Davis*, 2007 WL 2287889, at \*3 (E.D.N.Y. Aug. 8, 2007). If litigation is required to obtain payment, DOE may collect interest from the date of judgment until the loan is paid in full under 28 U.S.C. § 1961(a)<sup>8</sup> and costs of suit under 28 U.S.C. § 2412(a)(1)-(2). *See id.*

After PHEAA assigned the loan to DOE, Birch paid \$2,232.00. This amount was properly applied to interest rather than principal. As of September 21, 2009, Birch owed DOE \$60,689.73 in principal and \$27,552.94 in interest, a total of \$88,242.67. Interest at the rate of 9% has continued to accrue on the principal amount. Birch owes the principal amount and prejudgment interest directly to DOE. DOE is also entitled to recover postjudgment interest and costs of suit.

B. The Settlement Agreement

Birch also argues that PHEAA breached the settlement agreement when it failed to rehabilitate his consolidated student loan and waive collections costs, and but for the breach, Birch would owe DOE less than the amount calculated above. Under Pennsylvania law, a plaintiff asserting breach of contract bears the burden of proving: (1) the existence of a contract, including its essential terms; (2) breach of a duty imposed by the contract; and (3) damages. *Williams v. Nationwide Mut. Ins. Co.*, 750 A.2d 881, 884 (Pa. Super. Ct. 2000).

The parties do not dispute that Birch entered into a contract with PHEAA on September 5, 2002. The settlement agreement provided that if Birch made twelve monthly, consecutive payments of \$600, then PHEAA would rehabilitate his defaulted loan and waive collection costs from the date of rehabilitation forward. PHEAA's promise to rehabilitate the Birch loan and

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<sup>8</sup> Under § 1961(a), "[s]uch interest shall be calculated from the date of the entry of the judgment, at a rate equal to the weekly average 1-year constant maturity Treasury yield, as published by the Board of Governors of the Federal Reserve System, for the calendar week preceding."

waive collection costs was conditioned on Birch making monthly payments. Birch did not make payments every month, but paid over fourteen months. Since Birch did not perform his obligations under the settlement agreement, PHEAA did not have to rehabilitate the loan or waive collection costs. *See In re Columbia Gas System Inc.*, 50 F.3d 233, 241 (3d Cir. 1995) (“A contracting party’s failure to fulfill a condition excuses the performance by the other party whose performance is so conditioned . . . .”). Birch’s breach-of-contract claim fails because PHEAA did not breach a duty imposed by the settlement agreement.<sup>9</sup>

### **III. Conclusions of Law**

1. This court has jurisdiction over the parties and subject matter of this action under 28 U.S.C. § 1345. Venue is proper.

2. Birch’s federal consolidated loan was made under the Federal Family Education Loan Program (“FFELP”), 20 U.S.C. §§ 1071-1087.4, authorized under the Higher Education Act of 1965, 20 U.S.C. § 1071 *et seq.*

3. Birch defaulted on his consolidated student loan in the amount of \$60,689.73.

4. Since Birch did not perform his obligations under the settlement agreement, PHEAA did not have to rehabilitate the loan or waive collection costs.

5. Birch made payments totaling \$45,280.35 to PHEAA between the date of default and the date PHEAA assigned its claim to DOE on July 3, 2007. PHEAA properly applied the payments to collection costs and interest. The principal amount of \$60,689.73 was not reduced.

6. After PHEAA assigned the loan to DOE, Birch made payments to DOE totaling \$2,232.00. This amount was properly applied to outstanding interest. The principal amount of

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<sup>9</sup> PHEAA also argues that Birch’s breach-of-contract claim is barred by Pennsylvania’s statute of limitations. PHEAA did not breach the settlement agreement, so the court need not decide this defense.



\$60,689.73 was not reduced.

7. As of September 21, 2009, Birch owed \$60,689.73 in principal and \$27,552.94 in interest, a total of \$88,242.67. Interest has continued to accrue at the rate of \$14.96 per day for 365-day years and \$14.92 per day for 366-day years.

8. As of April 30, 2013, Birch owes a total of \$107,930.35 (principal plus prejudgment interest in the amount of \$47,240.62).

9. Birch is liable to DOE for his debt. Birch owes all future payments on the consolidated student loan to DOE.

10. DOE is entitled to collect interest from the date of judgment until the loan is paid in full under 28 U.S.C. § 1961(a) and costs of suit under 28 U.S.C. § 2412(a)(1)-(2).

Judgment will be entered accordingly.

**IN THE UNITED STATES DISTRICT COURT  
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<b>UNITED STATES OF AMERICA,</b>	:	<b>CIVIL ACTION</b>
<b>Plaintiff,</b>	:	
<b>v.</b>	:	
	:	
<b>ROBERT J. BIRCH,</b>	:	
<b>Defendant and Third-Party</b>	:	
<b>Plaintiff,</b>	:	
<b>v.</b>	:	<b>No. 10-1212</b>
	:	
<b>PENNSYLVANIA HIGHER</b>	:	
<b>EDUCATION ASSISTANCE AGENCY,</b>	:	
<b>Third-Party Defendant.</b>	:	

**JUDGMENT ORDER**

AND NOW, this 30th day of April, 2013, in accordance with the foregoing Findings of Fact and Conclusions of Law and Fed. R. Civ. P. 58, it is **ORDERED** that:

1. **JUDGMENT IS ENTERED** in favor of plaintiff, the United States of America, Department of Education, and against defendant Robert J. Birch in the amount of \$107,930.35, plus interest from the date of judgment until the loan is paid in full under 28 U.S.C. § 1961(a) and costs of suit under 28 U.S.C. § 2412(a)(1)-(2).

2. **JUDGMENT IS ENTERED** in favor of third-party defendant Pennsylvania Higher Education Assistance Agency and against third-party plaintiff Robert J. Birch.

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J.

